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No. 84-

IN THE SUPREME COURT OF THE UNITED STATES
October Term, 1984

THE COMMONWEALTH OF MASSACHUSETTS
by its DEPARTMENT OF PUBLIC WELFARE,
Petitioner,

v.

SECRETARY OF THE UNITED STATES
DEPARTMENT OF HEALTH AND
HUMAN SERVICES,

ADMINISTRATOR OF THE HEALTH CARE
FINANCING ADMINISTRATION,

and

THE DEPARTMENTAL GRANT APPEALS BOARD,
Respondents.

PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

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Issues Presented

1. Where the Commonwealth properly purchases nursing home care for the needy at interim rates in accordance with a Medicaid plan approved by the Secretary, is the Secretary authorized by the terms of the federal-state partnership agreement to refuse to reimburse the Commonwealth for the federal share of its unrecoverable expenditures in excess of the allowable costs of the nursing homes as later determined in final rates set in accordance with the plan?

2. Where the Court of Appeals found that the cornerstone provision of Title XIX, establishing the Commonwealth's right to reimbursement, is equivocal, did it err in deferring to the Secretary's contention, not embodied in

regulations, that Congress intended to permit her to determine retroactively and unilaterally not to pay the federal share of Medicaid funds properly expended by the Commonwealth in full compliance with its approved plan to purchase nursing home care for the needy?

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THE COMMONWEALTH OF MASSACHUSETTS
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SECRETARY OF THE UNITED STATES
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and

DEPARTMENTAL GRANT APPEALS BOARD,
Respondents.

PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FIRST CIRCUIT

The Commonwealth of Massachusetts hereby petitions this Court for a writ of certiorari to review a judgment of the United States Court of Appeals for the First Circuit.

Opinions Below

The opinion of the District Court is reported at 576 F. Supp. 1565 (1984), and is printed in the Appendix to the Petition (Pet. App.) at 41-56. The opinion of the Court of Appeals is reported at 749 F.2d 89 (1984), and is printed in the Appendix at 1-38. The Departmental Grant Appeals Board issued three opinions, of which the second, issued February 26, 1982, forms the subject matter of this petition. That opinion is printed in the Appendix at 57-122.

Jurisdiction

The judgment of the Court of Appeals for the First Circuit was entered on November 28, 1984. Pet. App. at 123. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

Statutes Involved

The statutory provisions involved are sections 1903 and 1905 of the Social Security Act, 42 U.S.C. §§ 1396b, 1396d. Pertinent portions of these statutes are reproduced in the Appendix to this Petition. Pet. App. at 124 et seq.

Statement of the Case

1. Title XIX of the Social Security Act (Medicaid), 42 U.S.C. §§ 1396 et seq., makes federal funds available to enable each participating state to furnish medical assistance, rehabilitation, and other services to needy persons. 42 U.S.C. § 1396. A state wishing to join in partnership with the United States for this purpose must submit a plan conforming to the specifications of 42 U.S.C. § 1396a (and the Secretary's elaboration of § 1396a in her regula-

tions) for the Secretary's approval.

Section 1396b(a) states the basic terms of the "contract", and § 1396b (a)(1) states the basic terms upon which the largest share of federal disbursements, those for medical assistance expenditures, are made. Under that section, once the state plan has been approved, the state is entitled to receive partial federal reimbursement for its expenditures under the plan.[1/]

1/ Section 1396b(a)(1) provides in part:

> (a) From the sums appropriated therefor, the Secretary (except as otherwise provided in this section) shall pay to each State which has a plan approved under this subchapter, for each quarter ...
>
> (1) an amount equal to the Federal medical assistance percentage ... of the total amount expended during such quarter as medical assistance under the State plan ....

While the list of statutory qualifications of this obligation has grown, the

(footnote continued)

Although participating states are allowed some discretion in choosing the types of services to be covered under their programs, they are required to cover certain types of services, including skilled nursing facility services. See 42 U.S.C. §§ 1396a(a)(10)(A), 1396d(a)(4) (1983). Massachusetts has chosen to cover intermediate care facility services as well. See 42 U.S.C. § 1396d(a)(15) (1983). For purposes of this petition, the Commonwealth will refer to both categories as nursing home services.

2. Under Title XIX of the Social Security Act, as it existed before 1980,[2/] three cardinal but potentially

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(footnote continued)

Secretary has not relied on any such qualification in these proceedings.

2/ Unless otherwise indicated, the Commonwealth will describe the Act as it existed before 1980, the relevant period for purposes of this petition.

conflicting principles governed nursing home reimbursement. First, the states were obliged to reimburse nursing homes "on a reasonable cost related basis, as determined in accordance with methods and standards which shall be developed by the State on the basis of cost-finding methods approved and verified by the Secretary." 42 U.S.C. § 1396a(a)(13)(E) (1979).[3/] The Secretary by regulation construed this provision to require that rates be sufficient "to reimburse in full the actual allowable costs of a facility that is economically and effi-

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3/ This provision was entirely rewritten in 1980, and was further amended and renumbered as § 1396a(a)(13)(A) in 1981. Pub. L. No. 96-499, § 962 (1980); Pub. L. No. 97-35, § 2173(a)(1) (1981). As rewritten, the provision affords the states additional leeway to devise reimbursement systems. The added discretion, however, does not diminish and may increase the states' jeopardy of a disallowance, if the Secretary's position in this case is sustained.

ciently operated." 42 C.F.R. § 447.302(b) (1979).

Second, while § 1396a(a)(13)(E) was understood to require full reimbursement of actual allowable costs, 42 U.S.C. § 1396b(i) (1979) provided that there would be no federal reimbursement for state expenditures exceeding the amount which would be paid for such care and services under the Medicare program, Title XVIII of the Social Security Act. See 42 C.F.R. §§ 447.252, .315, .316 (1979) (federal financial participation is available for expenditures which do not exceed the provider's customary charge or rates which would be paid using Medicare principles of reimbursement).

Third, to ensure the participation of providers, Title XIX requires prompt payment of invoices for care and services. See Massachusetts General Hospi-

tal v Sargent, 397 F. Supp. 1056, 1061-62 (D. Mass. 1975).[4/] See also 42 U.S.C. § 1396a(a)(37), as amended by Pub. L. No. 95-142, §§ 2(b)(1)(C), 3(c)(1)(C), 7(b)(1); 42 C.F.R. § 447.45(1979) (requiring payment of 90 percent of invoices submitted by individual providers or group practices within thirty days, and 99 percent within ninety days).

The Secretary has attempted to achieve these competing objectives for prompt, full, and accurate reimbursement by requiring payment at rates based on reported costs, subject to adjustment after an audit. See 42 C.F.R. § 447.302(b)(1979). This can be accom-

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4/ The court relied in part on the Secretary's Medicare regulations, which required "[i]nterim payments approximating the actual costs of the provider" to be made "not less often than monthly." 397 F. Supp. at 1061, quoting 20 C.F.R. § 405.454(a).

plished in one of two ways. Under a prospective reimbursement system, the rate for any year is derived from costs reported by the nursing home in an earlier year (the base year). No adjustment of the rate is subsequently made to reflect actual costs during the rate year, but the state conducts an on-site audit of the home to determine whether the home properly reported its costs during the base year and whether any nonallowable costs were included. A prospective rate may be adjusted retroactively based on the results of this audit.

Massachusetts and other states have opted to employ a retrospective ratesetting system,[5/] under which final per

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5/ The Commonwealth is informed that ten other states employ retrospective rate systems for one or more classes of providers. They are Florida, Idaho, Mis-

(footnote continued)

diem rates are established after the rate year based on the nursing homes' reports of their costs for the year. Such a system is a recognized option under the Secretary's regulations. See 42 C.F.R. § 447.272 (1979). However, because the final rate is not determined until well after the close of the rate year, the Secretary's regulations require Massachusetts to establish interim or estimated rates at the start of the year. In Massachusetts the interim rate is determined by adjusting the final rate for an earlier year to reflect inflation.6/

(footnote continued)

souri, New Hampshire, New Mexico, New York, Ohio, Oregon, Pennsylvania, and Wisconsin. In addition, Alabama, Nevada, and Virginia employ hybrid systems which are retrospective in part.

6/ Thus, the interim rate under Massachusetts's retrospective system corresponds to the final rate in a prospective system.

Because the interim and final rates are derived by different means from different base data, it is an inherent feature of a retrospective system that the interim rate will differ from the final rate.[7] If the final rate is higher than the interim rate, the Commonwealth must pay an additional amount to the nursing home equal to the rate differential times the total Medicaid patient days for the year. If the final rate is lower than the interim rate, the nursing home must repay the Commonwealth. The Commonwealth will refer to these latter claims as "rate decrease claims."[8]

7/ For instance, if the actual rate of inflation is lower than expected, the final rate will be lower because actual costs will be lower than predicted in the interim rate.

8/ The Commonwealth expends in excess of $400 million per year for nursing

(footnote continued)

In the usual case, the Commonwealth collects rate decrease claims either by deducting a percentage from current monthly payments to the nursing home, or by offsetting the claim against any lump sum payments which may be owing to the nursing home.9/ Because recovery of these claims and repayment of the federal share occurs promptly, this system ordinarily presents no problem. Occasionally, however, nursing homes go out of business or declare bankruptcy before a rate de-

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(footnote continued)

home services under the Medicaid program. If final rates deviated on average 5% from interim rates, and if one half of final rates were lower than the interim rates, the Commonwealth's system would generate $10 million in rate decrease claims per year. In fact, we are informed that, in 1980 and 1981, rate decrease claims were generated at the rate of about $12 million per year.

9/ Rate decrease claims are almost always collected from operating homes within one year. See Pet. App. 81.

crease claim has been established,[10/] or before it has been collected. For the most part such claims are uncollectible, in the case of bankrupt homes because they have been discharged by operation of federal law. In such cases, the question arises whether the Secretary may demand repayment of the federal share, thereby forcing the Commonwealth to bear the entire loss.

3. In 1979, agents of the Secretary audited the Commonwealth's financial records and determined that, as of September 30, 1979, the Commonwealth had outstanding rate decrease claims against bankrupt or out of business nursing homes

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10/ Plainly, because cost reports are filed after the close of the year, the final rate for the last year of a nursing home's operations could not be set before it ceases business or declares bankruptcy.

in the amount of $10,231,222.[11/] The federal share of these claims was said to be in excess of $5 million. Pet. App. at 64-65.

The Secretary's auditors did not find that the interim rates, upon which these payments had been made, were improperly calculated, or that any invoices were improvidently paid. On the contrary, the Secretary has assumed from the start that the interim rates were properly calculated, and has conceded for purposes of this case that all payments were made in accordance with the Commonwealth's plan, which the Secretary has approved. Nor has the Secretary alleged that these

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11/ This figure represented the accumulated total of unpaid claims from the inception of the retrospective system to the date of the audit. About $5.5 million consisted of claims against bankrupt nursing homes.

claims resulted from improper or inefficient administration; rather, they unavoidably arose as a byproduct of the Commonwealth's approved retrospective reimbursement system. Nor, finally, has the Secretary claimed that the interim rates at which the Commonwealth paid these nursing homes exceeded the upper limits established by Title XIX and the Secretary's regulations. See 42 U.S.C. §§ 1396a(a)(30), 1396b(i) (1979); 42 C.F.R. §§ 447.252, .315, .316 (1979).

Despite the fact that the Commonwealth had originally disbursed these sums properly, in accordance with its approved plan, and despite the absence of any regulation defining rate decrease claims as expenditures not entitled to

federal reimbursement,[12/] the Secretary's auditors alleged that the outstanding rate decrease claims in fact represented improper expenditures. Reasoning that these claims were determined by the Commonwealth to be overpayments to the nursing homes, the Secretary concluded that they were not "medical assistance" expenditures for which the Commonwealth was entitled to receive federal reimbursement. See 42 U.S.C. §§ 1396b (a)(1), 1396d(a). Accordingly, the Sec-

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12/ On April 5, 1983, the Secretary published proposed regulations which would spell out in some detail the states' obligations to identify and report overpayments to providers. 48 Fed. Reg. 14664 (April 5, 1983). Among other things, the regulations would define "overpayment" as "the amount, paid to a provider by a Medicaid agency, that HCFA determines to be in excess of the amount to which the provider was entitled," and would provide for recovery of the federal share of such overpayments whether or not the state recovers from the provider. Id. at 14667. The proposed regulations have not been promulgated.

retary demanded that the Commonwealth deduct the federal share of those claims immediately from the Commonwealth's next quarterly report of estimated expenditures, upon which federal reimbursement is based. See 42 U.S.C. § 1396b(d)(1).

On reconsideration of the Secretary's position, see 42 U.S.C. § 1316(d), the Grant Appeals Board (the Board), giving great weight to the Secretary's views, ruled that, to the extent an interim rate exceeds a final rate, payments at the interim rate are improper, and therefore do not qualify as expenditures for "medical assistance under the State plan," within the meaning of 42 U.S.C. § 1396b (a)(1). Federal payments to the Commonwealth based on such "improper" expenditures were, thus, overpayments which the Secretary was authorized by 42 U.S.C. § 1396b(d)(2) to deduct from subsequent

payments. Pet. App. at 67-73. On February 26, 1982, the Board issued its decision upholding the Secretary's authority in the circumstances, but leaving the amount of the disallowance to be resolved after further proceedings. Pet. App. at 121-22. That amount was ultimately fixed by the Board on June 30, 1983, at almost $4 million.

4. On April 22, 1982, the Commonwealth simultaneously filed a petition for review, pursuant to 42 U.S.C. § 1316(a)(3), in the United States Court of Appeals for the First Circuit, and this action in the District Court under 5 U.S.C. §§ 702, 703, and 28 U.S.C. § 2201, for judicial review of the Board's decision and for declaratory and injunctive relief against the Secretary. The jurisdiction of the District Court was founded upon 28 U.S.C. § 1331. This

action was stayed, on the Commonwealth's motion, pending decision of the petition in the Court of Appeals.

In January, 1983, the Court of Appeals determined that it did not have jurisdiction of the petition. Commonwealth of Massachusetts v. Departmental Grant Appeals Board, 698 F.2d 22 (1st Cir. 1983).[13/]

Following that decision, the parties filed cross-motions for summary judgment in the District Court. On January 12, 1984, that court (Garrity, J.) issued

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13/ The Court of Appeals stayed entry of its decree until the judgment of the District Court could be reviewed on appeal. The reason for the stay was a doubt as to whether the District Court had jurisdiction. The District Court found that it had jurisdiction. Pet. App. 47. Because the merits of the complaint were reached and decided by the courts below, the Commonwealth does not seek review of the decree of the Court of Appeals on the petition under 42 U.S.C. § 1316(a)(3).

its decision, and a judgment was entered the next day. Pet. App. 39-40.

The District Court disagreed with the Board's approach to the question, and reversed its decision. Given the Secretary's concession that the expenditures in issue had been made in accordance with the Commonwealth's approved plan, and the absence of any clear statutory or regulatory authorization to treat such expenditures as improper once a final rate had been determined, the District Court gave controlling weight to the overall character of the Medicaid program as a federal-state partnership. Pet. App. at 54, quoting Harris v. McRae, 448 U.S. 297, 308-09 (1981). Accordingly, the District Court held that the Commonwealth was not required to repay the federal share of its rate decrease claims except to the extent that those claims

were recovered from the nursing homes. Pet. App. at 54-55, citing 42 U.S.C. § 1396b(d)(3).

5. The Secretary appealed the judgment of the District Court and, on November 28, 1984, the Court of Appeals reversed. While it found that the terms of the statute could support either position, the Court of Appeals rejected the District Court's reliance upon the character of the Medicaid program as a partnership, since the court thought it equally consistent with such a relationship for the federal government to cast the entire burden of uncollectible claims on the Commonwealth. Pet. App. at 35-37.

The Court of Appeals also rejected the Commonwealth's argument that the Secretary's position was not clearly stated in the statute or in her regulations, and so was invalid. In the Court's view,

the "clear statement" rule articulated in Pennhurst State School & Hospital v. Halderman, 451 U.S. 1, 17 (1978),[14] is applicable to the determination of the existence vel non of conditions under a grant program, but not to the determination of the scope or application of a particular condition the existence of which is not in doubt. Pet. App. at 28-30. As to the latter issue, the Court of Appeals ruled that the Secretary's construction of the statutes was entitled to deference. Because the terms of the

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14/ We use the phrase "clear statement rule" as shorthand for the following passage in the Pennhurst decision:

> [I]f Congress intends to impose a condition on the grant of federal moneys, it must do so unambiguously. ... By insisting that Congress speak with a clear voice, we enable the States to exercise their choice knowingly, cognizant of the consequences of their participation.

451 U.S. at 17.

statute did not clearly support either position, the Secretary's construction of the statute was deemed determinative. Pet. App. at 32-35.

Reasons Why the Writ Should Be Allowed

I. THE DECISION BELOW MERITS REVIEW BECAUSE IT FUNDAMENTALLY DISTORTS THE RELATIONSHIP BETWEEN THE STATES AND THE UNITED STATES UNDER TITLE XIX.

The decision below puts questions of tremendous importance to the federal-state partnership authorized by Title XIX. Whether the Secretary must pay the federal share of expenditures required by an approved plan, or whether she may, on the contrary, refuse payment based on facts which were not reasonably knowable when the expenditures were made, is sufficiently important in itself to merit review and resolution by this Court, as

the Commonwealth will show in its next point.

But the Secretary's position strikes more deeply than the mere question of the Commonwealth's just expectation of reimbursement. While the Secretary has always exercised pervasive control over the formulation of state plans, through her power to interpret and fill out the provisions of § 1396a, and her power to approve or disapprove proposed plans and plan amendments, and while Congress has with increasing frequency provided incentives (or disincentives) to encourage accurate and efficient administration of state programs, it has always been thought that Title XIX authorizes partnerships, in which the states have discretion within known limits to adopt such systems as seem wise and appropriate for the achievement of the mutual goal of

furnishing medical assistance to the needy.

The Secretary's assertion of a general authority to refuse federal reimbursement for expenditures which she deems in hindsight to have been uneconomical or unnecessary, though they may be authorized or even required by the state's approved plan, belies any conception of Title XIX programs as a partnership. Not only does it repudiate any obligation to share the risks of the enterprise, but it also denies any obligation to identify in advance those risks which the federal government will not share, so that the states may avoid or minimize them.

The consequence is that, though the states may have discretion under federal law to design their programs as they see fit, neither the faultless operation of

the program, nor the Secretary's approval of its design will ensure that the federal government will share the program's cost. This is not discretion in the ordinary sense, for the asserted power denies all reliance or trust by the federal government in the states' management of their programs, even within the bounds of plans reviewed and approved in advance by the Secretary.

This was not Congress's intent in enacting Title XIX, as described by this Court, inter alia, in Harris v. McRae, 448 U.S. at 308-09.

Related to this question is the proper judicial approach to the resolution of disputes involving the basic rights and obligations of the states and federal government.

Both the District Court and the Court of Appeals concluded that the statute

itself is ambiguous on the issue presented in this case. The District Court resolved the dispute by giving determinative weight to the nature of Title XIX as a partnership. Pet. App. at 51, 53-54. The Court of Appeals, on the other hand, resolved the dispute by deferring to the Secretary's position. Pet. App. at 32-35.

The Commonwealth will argue in its third point that the question whether the Court of Appeals erred in adopting a stance of deference is one which this Court should review and decide. The Commonwealth observes here, however, that like the court's decision of the substantive issue, its approach to the interpretation of the statute seriously skews the relationship of the states to the federal government. To defer to the Secretary's post hoc definition of the fed-

eral obligation, and especially to defer to that interpretation on the ground that it is merely rational, that it can be said to further some end within the constellation of permissible governmental ends, is to transform a relationship which this Court has characterized as contractual in nature into a relationship between a regulator and regulatee.15/

In Bell v. New Jersey, 461 U.S. 773 (1983), Justice White identified these issues as matter for concern, id. at 794

15/ Of particular significance to the Court of Appeals was the additional fiscal protection that the Secretary's approach allegedly affords to the federal government, and the additional incentive it gives the states to operate their programs efficiently. Pet. App. at 35-37. The court's reliance on these objectives, and its lack of concern for whether the means chosen to achieve them were agreed to by the states, suggests that it viewed the issue as one concerning the rationality of an exercise of regulatory authority. The Secretary, too, has defended her position as if it were such an exercise.

(White, J., concurring), but the Court has not heard a case concerning the scope of the Secretary's disallowance authority before the current term. Three cases now pending before the Court present that issue in varying lights. See Kentucky Department of Education v. Secretary of Education, 717 F.2d 943 (6th Cir. 1983), cert. granted, 105 S. Ct. 78 (1984); State of New Jersey v. Hufstedler, 724 F.2d 34 (3rd Cir. 1983), cert. granted, 105 S. Ct. 79 (1984); State of Connecticut v. Heckler, 731 F.2d 1052 (2d Cir.), cert. granted, 105 S. Ct. 321 (1984). The Commonwealth suggests that the instant case may aid in clarifying the nature of the federal promise in spending power programs, and in the determination of the proper stance of a court reviewing a disallowance which is based upon a

nonobvious interpretation of a governing statute.

II. THE COURT'S HOLDING THAT STATES ARE NOT ENTITLED TO REIMBURSEMENT FOR EXPENSES PROPERLY INCURRED UNDER THEIR APPROVED PLANS IS AN IMPORTANT FEDERAL QUESTION WHICH SHOULD BE REVIEWED BY THIS COURT.

Congress enacted Title XIX in 1965 to encourage and assist the states to provide medical care to needy persons. See 42 U.S.C. § 1396. It chose to carry out this policy by proposing a partnership with each state, in which, in return for an agreement by the state to administer a program in conformity with federal specifications, the federal government would reimburse a portion of state expenditures under the program.

In Harris v. McRae, 448 U.S. 297, 308-09 (1981), this Court said that "the purpose of Congress in enacting Title

XIX was to provide federal financial assistance for all legitimate state expenditures under an approved Medicaid plan." The decision below challenges that view. On the record in this case, the Commonwealth did what was required of it by its approved plan and the Secretary's regulations. The Commonwealth's expenditures, judged as of the time they were made, were necessary and proper. Nevertheless, the Secretary has determined that she need not pay the full federal share of these expenditures, based on facts and circumstances which were not and could not have been known when the expenditures were incurred. The issue thus drawn is of profound importance to the administration of Title XIX.

Of course the decision of the Court of Appeals is of moment to the Commonwealth because of the sum involved, al-

most $4 million. But of greater moment is the decision's implication for the future. Because rate decrease claims are an inevitable feature of retrospective rate systems, the decision of the Court of Appeals ensures continuing losses of federal financial participation for so long as the Commonwealth employs such a system. Nor is this the concern of the Commonwealth alone. Retrospective rate systems are employed by ten other states,[16/] and the Secretary has already disallowed reimbursement to at least four of those states in reliance upon her reasoning in this case.[17/]

16/ The states are listed in footnote 5, supra.

17/ See Florida Department of Health & Human Services, Board Decision No. 296 (May 14, 1982) aff'd sub nom. State of Florida v. Heckler, Civil Action No. TCA

(footnote continued)

Furthermore, the decision below, while perhaps in keeping with the federal government's short-term financial interest, is not in harmony with the policies of Title XIX. First, since the decision below relieves the Secretary of any obligation to share even in inherent, foreseeable expenses under a state plan to the extent that they exceed the ideal

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82-0935 (N.D. Fla., January 5, 1984); Missouri Department of Social Services, Board Decision No. ___, rev'd sub nom. Department of Social Services v. Heckler, Civil Action No. 84-4106-CV-C-5 (W.D. Mo., September 10, 1984); New York State Department of Social Services, Board Decision No. 284 (April 29, 1982), aff'd, Perales v. Heckler, Civil Action No. 83-CV-900 (N.D.N.Y., October 1, 1984); Pennsylvania Department of Public Welfare, Board Decision No. 426 (May 24, 1983). About four months before its decision in the instant case, the Board upheld a similar disallowance in Ohio Department of Public Welfare, Board Decision No. 226 (October 30, 1981). The Board did not rely on that decision in this case.

level of expenditures, its effect is to decrease the federal government's share in the overall cost of furnishing medical assistance and to increase the state's cost. Given that available state funds are not inexhaustible, and that the state has the power to limit its expenditures by altering the design of its program, an increase in the state's share of the cost of furnishing services may provoke an offsetting decrease in the scope of the state's program, or of the services offered. Because federal funds are made available on a matching basis, the savings which the decision below may achieve in federal expenditures may well translate into fewer services for the needy. In this way, the Secretary's position that the states must bear alone some costs which cannot be avoided works against Congress's purpose to enable the

states "as far as practicable under the conditions in each State" to furnish medical assistance to the needy. 42 U.S.C. § 1396.

Second, while the Secretary and the Court of Appeals pay lip service to the states' role in the Medicaid program, and while both purport to recognize the freedom reserved to the states to fashion programs within the federal statutory framework, the decision in effect attaches a penalty (or negative incentive, as the Court of Appeals would have it, see Pet. App. at 36-37) to a program choice which otherwise complies with federal law. Congress has provided that the Commonwealth is entitled to receive partial federal reimbursement for its expenditures under its plan except as otherwise provided in § 1396b. A variety of provisions in § 1396b qualify that

premise. So, for instance, until 1981, § 1396b(i) provided that states would not be entitled to reimbursement for expenditures to the extent that they were made at rates exceeding what would be paid under Medicare. See also § 1396b (b), (f)-(m), (o), (r), (s), (u). But these explicit qualifications still leave room for the states to exercise their own judgment in fashioning programs to achieve the objectives of the Medicaid act. The decision below, however, permits the Secretary retroactively to impose financial constraints without explicit authority in § 1396b. In so doing, the decision authorizes the Secretary to control the states' exercise of the discretion left to them by Congress.

Third, although the Court of Appeals thought it reasonable to cast the entire risk of loss in a retrospective system

upon the Commonwealth,[18] this choice is likely to disserve congressional policy in the long run. For, the decision below could encourage inefficiency or noncompliance with the State plan. If rate decrease claims can only come into being when final rates are set, the decision below could encourage the states not to set such rates or to set them automatically at the same level as the interim rates for nursing homes which are not financially sound, or have already declared bankruptcy.[19] More

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18/ The court below recognized that the Commonwealth would be an equal partner in any loss, even if the court ruled in its favor, but thought that casting the entire loss on the Commonwealth would increase its incentive to operate its program efficiently. Pet. App. at 36-37.

19/ This is so because under the Secretary's scheme if a state recovers less than fifty percent of its claim in the bankruptcy court, it will be worse

(footnote continued)

broadly, because the risk of loss is greatest when the state exercises the strictest scrutiny of nursing home costs, the decision below discourages state initiatives to control such costs.

In its general aspect, the issue in this case is whether the Secretary may judge the legitimacy of state expenditures based on facts and circumstances which could not reasonably have been known when the expenditures were made. The question profoundly affects the "partnership" between the federal government and the states. If the Secretary is correct, then the relationship is one in which all risks, even inherent or un-

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(footnote continued)

off than if it had simply avoided the creation of a claim by setting the final rate at the same level as the interim rate.

avoidable risks, are borne by the states, and in which the Secretary, under the guise of her disallowance power, may second guess every aspect of a state's administration of its program.20/

So far as we are aware, this Court has not, prior to the current term, addressed the scope of the Secretary's power to define the federal reimbursement obligation and to disallow reimbursement for state expenditures in a cooperative

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20/ The Secretary has proposed regulations under which the legitimacy of state expenditures would depend on the Secretary's independent after-the-fact determination of rates for providers, even though the state may be required by state law or court decision to pay at a different rate. See 48 Fed. Reg. 14664 (April 5, 1983), discussed in footnote 12, supra. Indeed, the Secretary has asserted such authority in at least one disallowance. See South Carolina Department of Social Services, Board Decision No. 149 (February 3, 1981).

grant program.[21] The question has been considered by the lower courts,[22] and will recur with increasing frequency if it is not addressed and resolved by

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21/ The Court has frequently heard cases concerning the states' obligations under such programs. In Bell v. New Jersey, 461 U.S. 773 (1983), the Court considered the federal government's remedial options when a state misspends federal grant money. Justice White identified the scope of the disallowance power as an issue of concern, see id. at 794 (White, J., concurring), but the question has not been squarely presented before this term.

22/ See, e.g., California v. Settle, 708 F.2d 1380 (9th Cir. 1983) (Secretary need not reimburse erroneous payments under Title XIX even though they are practically unavoidable); County of Alameda v. Weinberger, 520 F.2d 344 (9th Cir. 1975) (Secretary may not disallow Title VI expenditures which are authorized by an approved plan, even though they allegedly violated the Secretary's regulations); Solomon v. Califano, 464 F. Supp. 1203 (D. Md. 1979) (Secretary may not disallow Title XIX expenditures which she has not shown to be inconsistent with an approved plan); Maryland v. Mathews, 415 F. Supp. 1206 (D.D.C. 1976) (Secretary may not disallow Title IV-A expenditures which, though theoretically excessive, were practically unavoidable).

this Court. It is urgently presented by the decision below. Accordingly, the Court should issue the writ to review the decision of the Court of Appeals.

III. THE COURT'S REFUSAL TO APPLY PENNHURST'S CLEAR STATEMENT RULE, AND ITS DEFERRAL TO THE SECRETARY'S POST HOC DENIAL OF A FEDERAL OBLIGATION TO THE STATES, RAISES AN IMPORTANT FEDERAL QUESTION WHICH SHOULD BE REVIEWED BY THIS COURT.

In Pennhurst, the Court observed that legislation such as Title XIX, which is enacted pursuant to the spending power, is "in the nature of a contract: in return for federal funds, the States agree to comply with federally imposed conditions." 451 U.S. at 17. Consequently, the Court said,

> The legitimacy of Congress' power to legislate under the Spending Power thus rests on whether the State voluntarily and knowingly accepts the terms of the "contract." ... There can, of course, be no knowing acceptance if a State is unaware of the

> conditions or is unable to ascertain what is expected of it. Accordingly, if Congress intends to impose a condition on the grant of federal moneys, it must do so unambiguously. ... By insisting that Congress speak with a clear voice, we enable the States to exercise their choice knowingly, cognizant of the consequences of their participation.

Id. at 17-18.

In the instant case, the Court of Appeals "[found] the statutory arguments presented on both sides equally balanced ...." Pet. App. at 32. The court refused, however, to apply the clear statement rule, and instead deferred to the Secretary's interpretation. The Court thought Pennhurst inapplicable to the resolution of minor or "interstitial" questions, or to the interpretation of existing conditions on the receipt of funds, as opposed to the determination whether a provision is a condition at all. Pet. App. at 29-30, 34. The court

found an analogy in Bell v. New Jersey, 461 U.S. 773, 790 n. 17 (1983), wherein this Court indicated that the Pennhurst rule might not be applicable to the determination of what remedies the federal government might have against states which concededly have misspent federal funds. Pet. App. at 30-31.

There is no merit to the court's suggestion that the dispute in this case concerns the remedies available to the federal government. To the contrary, the Commonwealth has assumed throughout this litigation that if it is not entitled to reimbursement under § 1396b(a) for its interim rate payments to nursing homes, then the Secretary may recover the federal share of those payments whether or not the Commonwealth makes recovery from the nursing homes. The dispute in this case thus concerns substantive

rights and obligations under § 1396b(a) -- the Secretary's obligation to pay, and the Commonwealth's right to be paid.

Further, contrary to the opinion below, this dispute does not concern a minor or interstitial question of law; rather, it concerns what this Court has identified as "the cornerstone of Medicaid," i.e., the availability of "federal financial assistance for all legitimate state expenditures under an approved Medicaid plan." Harris v. McRae, 448 U.S. at 308-09. As the Secretary's position and the decision below radically affect the obligation under § 1396b(a), they could scarcely cut more nearly to the core of this federal-state partnership.

In Bell v. New Jersey, 461 U.S. 773, (1983), the Court considered a claim that prior to 1978, the federal government

was without authority to recover funds under the Elementary and Secondary Education Act which had been misused by the states. While the Court found recoupment authority in the pre-1978 statute, it also suggested that the Pennhurst rule of construction might not apply to questions of remedy. Id. at 790 n. 17. That is very far from saying that the rule would not apply to questions of substantive right or obligation. Mr. Justice White noted the distinction and his own view that

> There is a significant issue whether a State can be required to repay if it has committed no more than a technical violation of the agreement or if the claim of violation rests on a new regulation or construction of the statute issued after the state entered the program and had its plan approved.

Id. at 794 (White, J., concurring). And, in Hendrick Hudson District Board of Education v. Rowley, 458 U.S. 176, 204 n.

26 (1982), the Court invoked the rule as an aid to determine the meaning of an acknowledged condition on federal grants under the Education for Handicapped Children Act, 20 U.S.C. §§ 1401 et seq.

Thus, the question whether the clear statement rule applies to the interpretation of statutory provisions establishing substantive conditions and obligations is a question which has been identified and which should be resolved by this Court.

The Court should resolve the question in this particular case for three additional reasons. First, it is exceptionally clear that the application of the rule would be dispositive of the case. The First Circuit repeatedly noted that the statute is ambiguous, and concluded that "the statutory arguments presented on both sides [are] equally balanced."

Pet. App. 23, 26, 32. Second, the underlying question is itself one of profound and lasting significance to the partnership established by Title XIX. See Argument I, supra.

Finally, the First Circuit's refusal to apply the clear statement rule appears to be in conflict with the view adopted by the Sixth Circuit in Kentucky Department of Education v. Secretary of Education, 717 F.2d 943 (6th Cir. 1983), cert. granted, 105 S. Ct. 78 (1984). There the Secretary of Education sought to recover funds paid under the Elementary and Secondary Education Act on the ground that they had been used in violation of a statutory condition that such funds not be used to supplant local funds. The court concluded that, although reasonable, the Secretary's test for whether federal funds had been used to supplant

local funds was not unambiguously supported by the statutes or regulations. Since the state's position was also reasonable under the statute, the Court reversed the Secretary's decision. Id. at 946-50.

If, as the Sixth Circuit held, the clear statement rule is applicable to the interpretation of an acknowledged grant condition,[23/] then the rule ap-

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23/ As previously noted, this Court has already invoked the rule as an aid in determining the meaning of an acknowledged grant condition. Hendrick Hudson Dist. Bd. of Educ. v. Rowley, 458 U.S. at 204 n. 26. The Kentucky case might be distinguished on the ground that the statute in Rowley was fundamentally ambiguous, while the ambiguity in the statute in issue in Kentucky concerned only the measure of compliance with a clear condition. But if such a distinction can be drawn, the instant case clearly falls on the Rowley side of the line, for there is no significant distinction between the imposition of a new condition, as in Pennhurst, or the imposition of a substantial new burden by interpre-

(footnote continued)

plies a fortiori in determining the extent of the Secretary's authority, if any, to disallow federal financial participation in expenditures authorized by a state plan. See also Perales v. United States, No. 83 Civ. 5850-CLB (S.D.N.Y., May 14, 1984), aff'd mem., No. 84-6249 (2d Cir., December 18, 1984) (declaring invalid, in the absence of clear statutory authorization, the assessment of interest against state agencies which delay repayment of federal funds under the Food Stamp program).

Not only did the Court of Appeals refuse to apply the clear statement rule, but it also determined that it was required to give the Secretary's interpre-

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(footnote continued)

tation of an acknowledged condition, as in Rowley, and the disavowal of the principal federal obligation under Title XIX, as in this case.

tation "significant weight." Pet. App. at 35. This element of the Court's decision also merits review by this Court.

In support of its decision, the Court of Appeals referred to the provision of § 1396b(d)(2) directing the Secretary to reduce payments on estimated state expenditures "to the extent of any overpayment ... which the Secretary determines was made." This provision, said the Court, "seemingly entrust[s] the determination of what constitutes an overpayment to the Secretary." Pet. App. 34 (emphasis added). But this amounts to a ruling that the Secretary is empowered to fix the federal government's substantive obligation to the states under § 1396b(a) after the states have already expended funds in accordance with their approved plans. Such a power is antithetical to the conception that a program such as

Title XIX is "in the nature of a contract." Pennhurst, 451 U.S. at 17. Indeed, the decision below in effect gives the Secretary the authority to "surpris[e] participating States with post-acceptance or 'retroactive' conditions," a power forbidden even to Congress. Id. at 25.

At bottom, the decision below betrays a confusion of the Secretary's roles under Title XIX. It may be granted that the Secretary enjoys regulatory authority under that program, but she exercises it in relation to the states only by virtue of their agreement to be so bound in return for partial federal reimbursement. The decision below enlarges this regulatory authority to include power to alter the very terms of the agreement from which the Secretary derives her authority.

Moreover, the decision compounds the confusion by giving retrospective effect to an exercise of regulatory control in a dispute over the Secretary's obligation to reimburse costs previously incurred. But as the court itself recognized, deference to the Secretary's views, not memorialized in regulations, is problematical in the context of a disallowance proceeding. See Pet. App. at 35. In that context, the Secretary's regulatory goals, if any, are subordinated to her pecuniary interest. It can scarcely be said that the retroactive imposition of a nonobvious interpretation upon the states, in a dispute over money, furthers a regulatory goal.[24/] See Kentucky De-

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24/ Furthermore, § 1396c appears to contemplate that such changes in federal policy be effectuated prospectively, as is usual with regulatory action. See

(footnote continued)

partment of Education v. Secretary of Education, 717 F.2d at 947 (in disallowance proceeding, reasonableness of Secretary's interpretation is not relevant; fairness to the state requires that such interpretation be given purely prospective effect).

Because the lower court's evident confusion concerns the "cornerstone" of Title XIX, see Harris v. McRae, 448 U.S. at 308-09, the question whether that court erred in refusing to apply the clear statement rule, and in deferring to the Secretary, merits review by this Court.

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County of Alameda v. Weinberger, 520 F.2d 344 (9th Cir. 1975); Solomon v. Califano, 464 F.2d 1203 (D. Md. 1979).

Conclusion

For the reasons stated, the Court should issue a writ of certiorari to review the judgment of the United States Court of Appeals for the First Circuit.

Respectfully submitted,

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